Supreme Court, U. S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-509

MARTIN G. ROSANSKY,

Petitioner,

v.

LADENBURG, THALMANN & CO., INC.,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE APPELLATE DIVISION, FIRST DEPARTMENT OF THE SUPREME COURT OF THE STATE OF NEW YORK

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To The Honorable The Chief Justice And Associate Justices Of The Supreme Court Of The United States:

Petitioner prays that a writ of certiorari be issued to review the judgment of the Appellate Division, First Department, of the Supreme Court of the State of New York in the above entitled action.

OPINION BELOW

Neither the Court of Appeals nor the Appellate Division, First Department, of the Supreme Court of the State of New York rendered an opinion. The opinion of the Supreme Court of the State of New York is unreported. A copy of this opinion is annexed hereto as Appendix A.

JURISDICTION

The jurisdiction of this Court is invoked under 28 United States Code, Section 1257 by reason of the fact that the Court of Appeals of the State of New York, as the Court of last resort, refused to grant leave to appeal and thus left standing a decision of the Appellate Division, Supreme Court, affirming an arbitration award based on a proceeding in which there was introduced, over the objections of petitioners, a counterclaim arising under the Securities Exchange Act of 1934,

15 U.S.C. 78aa ("1934 Act"), that act provides, in pertinent part, that:

> "The district court of the United States, and the United States courts of any territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder. (Emphasis added)

QUESTION PRESENTED FOR REVIEW

Did the New York Court err in confirming an award of an arbitration panel acting pursuant to the New York Arbitration Act in a proceeding instituted by petitioner, a customer of respondent (a member of the National Association of Securities Dealers) for non-payment for securities sold for petitioner's account, which panel, over petitioner's objection

(a) held that it had jurisdiction to hear and decide a counterclaim of

respondent based upon alleged violations by petitioner of the 1934 Act; and

(b) heard extensive evidence of such alleged violations of the 1934 Act; and

(c) thereafter dismissed petitioner's claim and respondent's counterclaim.

STATEMENT

The proceedings below were commenced by the filing by petitioner of an arbitration "Submission Agreement", dated May 13, 1974, under the Code of Arbitration Procedure ("CAP") of the National Association of Securities Dealers ("NASD").

Petitioner, an officer of Power Conversion, Inc. ("PCI") initiated the arbitration with respect to a $20,000 claim for breach of contract for the sale of 500 shares of PCI common stock for which respondent, the purchaser, refused to pay.

After the arbitration proceedings had been commenced, respondent interposed a counterclaim against petitioner for

$200,000 asserting a violation of Rule 10b-5 promulgated pursuant to the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.).

Petitioner challenged the jurisdiction of the arbitration panel to entertain the said "counterclaim" under NASD-CAP. The panel did not initially decide the jurisdictional objection. After hearing the evidence on the claim which consisted simply of the respondent's "confirmation" of the sale, the arbitrators heard extensive evidence of the alleged violation of petitioner of the 1934 Act, and then rendered a decision

(a) holding that the panel had jurisdiction over the 1934 Act counterclaim; and

(b) dismissing both the claim and counterclaim.

Petitioner thereafter moved in Supreme Court, New York County under New York CPLR 7511 to vacate the award on the ground that, inter alia the arbitrators,

in entertaining the respondent's counter-claim and hearing evidence with respect thereto exceeded their power. That Court denied the motion and confirmed the award. Thereafter petitioner appealed to the Appellate Division, First Department, of the Supreme Court seeking a reversal of the Supreme Court's order confirming the award. That Court affirmed the Supreme Court's judgment without an opinion. Petitioner then moved the Supreme Court, Appellate Division for an order granting a rehearing or leave for appeal to the Court of Appeals of the State of New York. CPLR 5602. The Court denied both motions. Thereafter petitioner moved the Court of Appeals for an order granting leave to appeal to the Court of Appeals. CPLR 5602. On July 7, 1977, the Court of Appeals denied the motion thus exhausting the remedies available to petitioner under New York law and procedure.

REASONS FOR GRANTING THE WRIT

A.

The decision below squarely presents an important Federal question -- never passed upon by this Court -- as to whether any claim under the 1934 Act is arbitrable, with or without the consent of the parties.

After forty years, there still exists an important and unanswered question as to whether any claim arising under the 1934 Act is arbitrable. In spite of the tremendous impact that that Act has had on the securities industry and its customers, neither can be sure whether it has a judicial or arbitral remedy under the Act. This court has never passed on the question of whether a 1934 Act claim is arbitrable. This unsettled state of affairs should not continue and this Court is respectfully requested to issue the writ sought and allow this question to be fully briefed and squarely presented for adjudication.

In the preamble of the Act, section 2 states:

> "[S]ecurities exchanges and over-the-counter markets are affected with a national public interest...."

Inasmuch as the Act is an expression of statutory public policy, the comment of Judge Charles E. Clark in his dissenting opinion in Wilko v. Swan, 201 F.2d 439 (2nd Cir.) whose position was ultimately sustained by this Court, 346 U.S. 427 (1953) is particularly germane. Judge Clark pointed out the dangers of permitting commercial arbitration to extend its reach into areas involving public policy:

> "Commercial arbitration has been highly successful in bringing a businessman's adjudication to business questions. But it would be vastly unfortunate if it became usable as a device to blunt or break social legislation." (201 F.2d at 445)

In Wilko v. Swan, 346 U.S. 427 (1953) the petitioner sued to recover damage pursuant to the Securities Act of 1933.

The Court held that an agreement to arbitrate a future controversy was void under the 1933 Act. This Court did not there hold, nor has it ever held since, that a different rule prevails with respect to existing controversies. The Court of Appeals of the Third Circuit has held that, under certain extreme circumstances, a party might waive right to have 1934 Acts decided by a Court (Moran v. Paine, Webber, Jackson & Curtis, 389 F.2d 242 (3rd Cir. 1968); however, the decisions of the District Court of the Southern District of New York (Pollock, J.) in Sobel v. Hertz Warner & Co., 338 F.Supp. 287 (1971) and the Second Circuit, in reversing and remanding (469 F.2d 1211 (1972)) clearly point up the inherent problems in permitting a 1934 Act claim to be submitted to arbitration, discussed infra.

This Court, in Wilko v. Swan, took specific note of the many problems in arbitrating 1933 Act claims which apply with equal force to 1934 Act claims (Axelrod &

Co. v. Kordich, Victor & Newfeld, 451 F.2d 838, 843 (2nd Cir. 1971)). Such claims require subjective findings on the purpose and knowledge of the alleged violator. Such findings by an arbitration panel would necessarily be determined and applied without judicial instruction. In addition they are almost always decided without explanation or complete records. This makes effective judicial review well nigh impossible (the problem "wrestled with" but not determined in Sobel, supra). These considerations which were held to be fatal to the arbitrability of a 1933 Act claim are equally important under the 1934 Act.

In Sobel, supra, a customer who agreed to arbitrate an existing dispute under the 1934 Act and lost his claim before the arbitrators, moved the district court to vacate the award. The district court faced with no record of how the panel arrived at its decision ordered the case remanded to the panel for explanation. The Court of

Appeals reversed and remanded holding that the efficiency and informality of arbitration would be destroyed under such procedure; after discussing the conflicting public policy questions (desirability of arbitration vs desirability of correct decisions in the 1934 Act cases) the Court, as noted above, reversed and remanded, holding:

> "In short, we believe that the district court erred in remanding the arbitration proceeding to the arbitrators. We do not agree with its conclusion that 'the present state of the record is not sufficient to justify final determination of the issues petitioner has raised.' 338 F.Supp. at 289. Those issues are whether the arbitration award was procured by 'undue means,' 9 U.S.C. §10(a), or is void as against public policy. Both parties have urged us to decide those questions. While we are tempted to do so in order to bring this litigation to an end, orderly administration suggests that the district court should rule upon them first." (469 F.2d at 1216)

Petitioner herein is faced with a similar problem and understands that if arbitrators simply ignore applicable law or exceed their power then such action would compel vacation of the award. Petitioner submits that arbitration should not be used to decide 1934 Act claims because judicial review is effectively thwarted.*

B.

The State Court decided an important question of Federal law for the first time, in a manner not in accord with the 1934 Act and probably not in accord with decisions of this Court, that if 1934 Act questions

*Petitioner, of course, is aware of the numerous decisions of Courts of Appeals upholding arbitration of disputes between brokers and members of brokerage firms. Those cases are founded upon a specific statutory recognition of agreements to settle disputes between securities exchange members (1934 Act §28(b)). See e.g. Axelrod & Co. v. Kordich, Victory & Newfeld, 451 F.2d 838 (2nd Cir. 1971) and cases and authorities there discussed.

may under proper circumstances, be submitted to arbitration, must such arbitration be conducted under the Federal Arbitration Act under the aegis of Federal Courts or may such arbitration be conducted under the State Arbitration Act under the aegis of the State Courts.

The Securities Exchange Act of 1934 confers exclusive jurisdiction on the federal judiciary to hear all cases arising under that statute:

> "The district courts of the United States...shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder." (15 U.S.C. 78 aa) (Emphasis added)

The federal courts have repeatedly sustained their right to exclusivity. Clark v. Watchie, 513 F.2d 994 (9th Cir.) cert. den. 423 U.S. 841 (1975);

Wright v. Securities and Exchange Commission, 112 F.2d 89 (2nd Cir. 1940). Even the courts of the State of New York have historically recognized that the federal courts have pre-empted this area of regulation. New York Stock Exchange v. Goodbody & Co., 42 A.D.2d 556, 345 N.Y.S.2d 58 (1st Dept. 1973) (defenses and counterclaims involving Securities and Exchange Act of 1934 were not cognizable in the state court).

In spite of the clear wording of the statute and rulings by both federal and state courts, the New York Court below clearly did not consider itself so limited in the case of arbitration of 1934 Act claims as it confirmed the arbitrator award rather than refusing to accept jurisdiction.

It is respectfully submitted that even if such claims are arbitrable under proper circumstances, any such arbitration must be conducted under federal and not state

arbitration procedures. The reason why petitioner moved in the State Court to vacate the award is that no Federal question was presented by petitioner's claim; since petitioner was challenging the right of the arbitrators to hear the counterclaims arising under Federal law it would have been totally inconsistent for petitioner to invoke the jurisdiction of the Federal Court to deny jurisdiction of Federal question.* Cf. Metro Indust. Painting Corp. v. Terminal Const. Co., 287 F.2d 382 (2nd Cir. 1961). Petitioner's dilemma was that he was challenging the jurisdiction of the arbitrators to hear the counterclaims based on exclusively Federal questions; had petitioner invoked the jurisdiction of the Federal Court he would have expressly (or tacitly) been asserting that that Court had jurisdiction which, in turn, would necessarily have been founded on

*Quaere: Where arbitration is invoked under a question of state law and a counterclaim is interposed of an exclusive Federal question; under which arbitration act are the parties proceeding; the State or the Federal?

the proper existence of a Federal question before the arbitrators -- the very point which petitioner was challenging.

In any event, it is respectfully submitted that the State Court, in confirming the award of the arbitration panel, necessarily held that

(1) the State Court had jurisdiction over an arbitration of 1934 Act claims; and

(2) the State arbitration act controlled such arbitration.

In the light of the express provisions of the 1934 Act that the Federal Courts have exclusive jurisdiction over claims in law or in equity under the 1934 Act, it is respectfully submitted that the New York Courts have, in this case of first impression, incorrectly decided this important question of Federal law.

C.

The State Court decided an important question of Federal law for the first time in a manner probably not in accord with the decisions of this Court, in that it permitted the arbitration of a 1934 Act claim against petitioner, which was not previously known to petitioner, over the specific and continual objection of petitioner.

Here, petitioner sold stock through his broker, E.F. Hutton, to respondent. Respondent refused to pay the $20,000 due as the purchase price and petitioner commenced what he contemplated was to be a simple arbitration under the CAP of the NASD.

After invoking the jurisdiction of the arbitrators, petitioner was confronted for the first time with a $200,000 counter-claim based upon claimed violations of the 1933 and 1934 Acts (there is involved here

only the question of the 1934 Act claims, but the point is exactly the same with respect to the 1933 Act claims asserted).

Petitioner objected to the counterclaims and the arbitrators reserved decision.

After presentation of petitioner's case, which consisted of a very short presentation of the facts and the introduction of the respondent's "confirmation" of the purchase, respondent was permitted to go on for days alleging all types of alleged violations of the 1933 and 1934 Acts.

Thereafter, the arbitrators held that they had jurisdiction of the 1933 and 1934 Act counterclaims, and dismissed both the petitioner's claim and respondent's counterclaim.

Of course, no one can say with assurance the extent to which the allegations of the 1934 Act violations affected the decision of the arbitrators on the petitioner's claim, but the point is that

they never should have been permitted to hear such allegations.

It is respectfully submitted that the clear holding of this Court in Wilko v. Swan, supra, has been violated under the procedural ploy that once petitioner invoked the jurisdiction of the arbitrators on his simple claim for money damages he consented to any and all counterclaims, including unknown claims under the 1933 and 1934 Acts.

Certainly, the facts of this case do not meet the standards of Moran v. Paine, Webber, Jackson & Curtis, supra, which is a Circuit Court exception to the rule of Wilko v. Swan.

It is respectfully submitted that even if such be the law of New York with respect to normal arbitration procedures, State procedural rules under State arbitration acts cannot be permitted to deprive a party of a substantive Federal right to a hearing of 1934 Act claims by a Federal Court.

WHEREFORE, petitioner prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the Appellate Division, First Department of the Supreme Court of the State of New York commanding that Court to certify and send to this Court for its review and determination on a date certain to be therein named, a full and complete transcript of all proceedings of the case entitled on its docket No. 08566/76, Martin G. Rosansky, Petitioner - Appellant, against, Ladenburg, Thalmann & Co., Inc., Respondent-Respondent; and that said decree of the Appellate Division, First Department, of the Supreme Court of the State of New York be reversed by this Honorable Court, and that your petitioner may have such other and further relief on the premises as to this Court may seem just and proper.

Dated: New York, New York

Respectfully submitted,

Martin G. Rosansky, Petitioner
By Richard deY. Manning

APPENDIX A

SUPREME COURT OF THE STATE OF NEW YORK,
SPECIAL TERM, PART I, NEW YORK COUNTY
at the Courthouse thereof, 60 Centre
St., New York, New York, 10007

Present:
HON. HAROLD BAER
Justice

———————————————x

MARTIN G. ROSANSKY

-against-

LADENBURG, THALMANN & CO., INC.

———————————————x

The following papers numbered 1 to 21 read on this motion SUBMITTED

No 283 on Calendar of May 20, 1976	PAPERS NUMBERED
Notice of Motion-Order to Show Cause-and Affidavits annexed	1-10
Answering Affidavit-Cross Motion	11-19
Replying Affidavit	20
Affidavit	21

Upon the foregoing papers this motion for an order vacating arbitrator's award is denied and the cross motion for an order

confirming same together with judgment in accordance therewith is granted.

Whether respondent's counterclaim was related to petitioner's claim was properly reserved for the arbitrators' determination. In the absence of a clear exclusion from arbitration, which is not the case here, questions concerning arbitrability are properly resolved at the arbitration, not in a court. Settle order.

Dated: June 25, 1976

H.B.
J.S.C.

County Clerk's No. 8566, 1976
Spec I Liber R61, Line 9, 1976